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No. 81-2409

In the Supreme Court of the United States

OCTOBER TERM, 1981

SECURITY GAS & OIL INC.,
a California corporation,
RAYMOND G. MILLER, EMANUEL RAPOPORT
AND
JAMES BARRONS,
PETITIONERS,

v.

JOSEPH KRAMAS,
RESPONDENT.

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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Respondent Joseph Kramas respectfully requests that this Court deny the Petition for Writ of Certiorari seeking review of the Ninth Circuit's judgment in this case.

Reasons Why The Writ Should Be Denied

I. The Court of Appeals followed the Law as Established by this Court.

II. There is no Conflict among the Circuits Concerning the Definition of Materiality.

III. The Court of Appeals followed Long Established Precedents in Holding that the Kramas Objection was Sufficient to Alert the Court to Error.

I. THE COURT OF APPEALS FOLLOWED THE LAW AS ESTABLISHED BY THIS COURT.

The Court of Appeals properly held that the District Court's instructions in an omission case were erroneous and contrary to this Court's holding in *Affiliated Ute Citizens of Utah* v. *United States*, 406 U.S. 128 (1972). In its instructions to the jury, the District Court stated the following concerning omissions:

> A fact omitted to be stated is the kind of thing that a reasonable person would have changed his mind about had he known the true fact.

Kramas v. *Security Gas & Oil Inc.*, 672 F.2d 766, 768, (9th Cir. 1982).

Three pages later in the transcript after the instructions on materiality, the court instructed the jury on reliance as follows:

> The burden in that case, I would think would be that the plaintiff would show that his decision would have been different had he been made aware of the fact omitted in the presentation.

Id. at 769 n.1.

Plaintiff's counsel objected to the implication in the trial court's instruction. Specifically, counsel noted the following:

> COUNSEL: Your Honor, I would only object to the language stated by the Court concerning the reliance being that it would have dissuaded the plaintiff from investing. I don't believe that to be the law.

> I think, as I understand the law, to be sufficient so that he would have considered it; but that the law does not say, requirement of dissuading him from investing.

Id. at 769.

The Court of Appeals found the instruction erroneous because it implied that the plaintiff must prove reliance upon an alleged omission by showing actual influence upon behavior. The instruction, the Court of Appeals properly noted, was directly contrary to this Court's holding in *Affiliated Ute* wherein this Court specifically stated:

> Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision.

Affiliated Ute Citizens of Utah v. *United States*, 406 U.S. at 153-54.

The Court of Appeals also held that the trial court instruction on materiality, as it related solely to misrepresentations, was wrong and contrary to this Court's holding in *Affiliated Ute* and *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438 (1976). In defining a material fact in the case of a misrepresentation, the trial court instructed the jury as follows:

> In the case of the matter stated, is it the sort of thing that, if stated correctly, would have dissuaded the investor from the making the investment [?]

Kramas v. *Security Gas & Oil, Inc.*, 672 F.2d at 768. In *TSC Industries*, however, this Court specifically rejected such an approach:

> The question of materiality, it is universally agreed, is an objective one, involving the significance of an

> omitted or misrepresented fact *to a reasonable investor.* Variation in the formulation of a general test of materiality occurs in the articulation of just how significant a fact must be or, *put another way, how certain it must be that the fact would affect a reasonable investor's judgment.*
>
> ....
>
> As an abstract proposition, the most desirable role for a court in a suit of this sort, coming after the consummation of the proposed transaction, would perhaps be to determine whether in fact the proposal would have been favored by the shareholders and consummated in the absence of any misstatement or omission. But as we recognized in *Mills, supra,* at 382 n.5, 90 S.Ct. at 620, such matters are not subject to determination with certainty.

TSC Industries, Inc. v. *Northway, Inc.*, 426 U.S. at 445 & 448.

(Emphasis added.)

As noted by the Court of Appeals:

> The definition of materiality is the same whether misrepresentations or omissions are involved, and as the Supreme Court said in *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449, 96 S. Ct. 2126, 2132, 48 L.Ed.2d 757 (1976), this standard 'does not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote.'

Kramas v. *Security Gas & Oil Inc.*, 672 F.2d at 769, quoting from *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449 (1976). See also *Affiliated Ute Citizens of Utah* v. *United States*, 406 U.S. at 153-54.

It is somewhat difficult to discern Petitioners' argument in requesting this Court to grant certiorari. Petitioners are constantly skipping between reliance and materiality, never clearly distinguishing between the two. For example, Petitioners state:

> The District Court's instruction that *reliance* must be such that an investor would have been dissuaded from making an investment in the case of misrepresentations was entirely in keeping with case law. The Ninth Circuit itself has adhered in 10b-5 cases to the traditional and less speculative common law of the objective test of *materiality*.

Petitioners' Writ at 8 (emphasis supplied). And again, in Petitioners' concluding argument, they state:

> Clearly, then, it is the law among the various circuits, including the Ninth Circuit, that in order for a misrepresentation to be deemed *material*, it must be established that the investor would have acted differently had the facts been truthfully stated. . . . Again, it is another way of saying that *reliance* on the part of the investor is a requirement under Rule 10b-5 in the case of misrepresentations.

Petitioners' Writ at 10 (emphasis supplied).

Petitioners are apparently arguing that materiality and reliance are one and the same element. *Id.* Petitioners' argument stems from a misconception and confusion of the elements of materiality and reliance. Materiality relates to the issue whether a resonable investor would consider the omitted or misstated facts important in making an investment decision. The test is intended to exclude trivial, albeit relevant, facts or facts tangentially related to the fraud, which are therefore unnecessary to a reasonable investor in the formation of the decision to invest. Reliance, on the other hand, is concerned with whether the individual plaintiff believed that the misrepresented statement was true. 5A A. JACOBS, LITIGATION AND PRACTICE UNDER RULE 10b5, §§61.02[a] and 64.01[a] (1982).

What is important to note, however, is that neither the District Court nor the Court of Appeals were ever faced with or addressed the issue whether materiality is equated with reliance in a misrepresentation case. *Kramas* v. *Security Gas & Oil Inc.*, 672 F.2d at 769 n.2. The only reliance issue raised and addressed was whether actual reliance need be established with respect to omissions. Petitioners, however, specifically refused to address that issue. Petitioners' Writ at 8.

II. THERE IS NO CONFLICT AMONG THE CIRCUITS CONCERNING THE DEFINITION OF MATERIALITY.

Petitioners argue, without citing a single case, that "clearly the circuit courts, in the event of misrepresentations, adhere to a requirement that materiality be founded upon the concept that *the investor* would have acted differently had he known the true fact." Petitioners' Writ at 9. As noted, such a result would be contrary to this Court's rule, as established in *TSC Industries* and *Affiliated Ute*, that the facts withheld or misstated be material in the sense that a reasonable investor would have considered them important in making the investment decision. The Ninth Circuit and other circuits addressing the issue subsequent to *TSC Industries* have applied the test as established by this Court. There is no disagreement either between the circuit courts and this Court, or among the circuits. *See SEC* v. *Washington County Utility District*, 676 F.2d 218 (6th Cir. 1982); *SEC* v. *Falstaff Brewing Company*, 629 F.2d 62 (D.C. Cir.), *cert. denied* 449 U.S. 1012 (1980); *Healy* v. *Catalyst Recovery of Pennsylvania, Inc.*, 616 F.2d 641 (3d Cir. 1980); *SEC* v. *Mize*, 615 F.2d 1046 (5th Cir.), *cert. denied* 449 U.S. 901 (1980); *Goodman* v. *Epstein*, 582 F.2d 388 (7th Cir. 1978), *cert. denied* 440 U.S. 939 (1979); *Zweig* v. *Hearst Corp.*, 459 F.2d 1261 (9th Cir. 1979); *Holmes* v. *Bateson*, 583 F.2d 542 (1st Cir. 1978); *St. Louis Union Trust* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 562 F.2d 1040 (8th Cir.), *cert. denied* 435 U.S. 925 (1978); *Hassig* v. *Pearson*, 565 F.2d 644 (10th Cir. 1977); *SEC* v. *Research Automation Corp.*, 585 F.2d 31 (2d Cir. 1973).

III. THE COURT OF APPEALS FOLLOWED LONG ESTABLISHED PRECEDENTS IN HOLDING THAT THE KRAMAS OBJECTION WAS SUFFICIENT TO ALERT THE COURT TO ERROR.

The Court of Appeals followed the other circuits, as Petitioners concede, by adopting and applying a long respected doctrine in its interpretation of Federal Rule of Civil Procedure 51: An objection which alerts the court to error satisfies the rule. *Kramas* v. *Security Gas & Oil Inc.*, 672 F.2d at 769.

As discussed above, the definition of materiality is the same whether misrepresentations or omissions are involved. The District Court in its charge to the jury misstated that definition and Kramas objected to the Court's language concerning whether the omitted or misrepresented facts would have dissuaded the investor from making the investment. Petitioners' argument appears to be that Kramas' objection was not sufficient because it could have related either to the definition of materiality as it relates to an omission or misrepresentation. Petitioners' Writ at 6. As discussed above, however, the law established by this Court is that the test of materiality is the same as to omissions as well as misrepresentations.

It does not help the Petitioners to rely upon *Palmer* v. *Hoffman*, 318 U.S. 108 (1943). In *Hoffman*, the objection related to the burden of proving contributory negligence when two separate causes of action were based on common law and two on statutory law. The trial court in *Hoffman*, without distinguishing between the various causes of action, charged that plaintiff had the burden of proving contributory negligence. The plaintiff objected, generally, to the instruction, without distinguishing the causes of action. The instruction was correct as it related to the statutory cause of action, but not to the common law causes of action. Because the instruction was correct in part, this Court stated that a general objection was not sufficient if a party might have obtained a correct charge by specifically calling attention to the error to the trial court. *Id.* at 119. In short, this Court looked at the issue whether it would be fair to the parties involved to allow a general instruction.

Unlike the *Palmer* case, the instruction given by the District Court in this case with respect to materiality was incorrect as to either omissions or misrepresentations, and Kramas could have said nothing more to convince the trial court to correct the instruction. Thus, the purpose of the Rule, to enable the trial judge to avoid error in his charge, was met and no purpose would have been served by requiring pointless formalities.

CONCLUSION

For the reasons stated, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

October 28, 1982

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